

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In ,the Matter of the Appeal of)
HALLIE L. BILLS)

For Appellant: Hallie L. Bills, in pro. per.

For Respondent: Burl D. Lack; Chief Counsel;
Israel Rogers, Associate Tax Counsel

OPINION

This appeal is made pursuant to section 19059 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claims of Hallie L. Bills for refund of personal income tax in the amounts of \$226.58 and \$103.52 for the years 1960 and 1961, respectively.

The sole question presented here is: 'Under section 18001 of the Revenue and Taxation Code, is appellant entitled to a credit for income tax paid to the State of Montana on interest income derived from promissory notes held by him in connection with his sale of real estate located in Montana?

For many years prior to 1960 appellant had resided in Montana, where he owned and operated a ranching business. In October 1959, he sold the ranch, receiving a cash down payment and the buyer's interest-bearing promissory notes for the remainder of the purchase price, which was to be paid in installments. Soon after the sale of his Montana property, appellant became a resident of California.

Appellant filed nonresident income tax returns with the State of Montana for the years 1960, and 1961, in which he reported as income the gain realized on the sale of his ranch located in that state. In his Montana returns appellant did

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not include in income the interest received on the buyer's promissory notes, which he then held in California. Appellant filed California resident income tax returns for the years 1960 and 1961, and in those returns he reported and paid tax on the interest income received on the notes, but not the gain realized on the sale of his ranch.

The Montana Board of Equalization notified appellant that the interest which he had received on the notes should have been included in his gross income, for purposes of determining the income tax due to Montana. This **conclusion** was based on an-administrative interpretation of the following Montana income tax statute:

In the case of a taxpayer other than a resident of this state, adjusted gross income includes the entire amount of adjusted gross income from **sources** within this state, but shall not include ... interest on bonds, notes or other interest-bearing obligations, ... **except to the extent to which the same** shall be a part of income from any business, trade, profession or occupation carried on in this state.... (Mont. Rev. Codes Ann. § 84-4907 (1947).)

The Montana taxing authorities consider a **sale** of business property **to be** a business, and the seller is deemed to be **in** the "business of selling a business" until the terms of the contract have been completed. Interest **received** on an installment contract is held to be directly related to such business, and is therefore included in the nonresident seller's adjusted gross income under the above quoted section.

Appellant paid the deficiency assessed by Montana. Since he had reported and paid tax on the same interest income in his California tax returns, appellant filed claims for refund with **respondent** in which he claimed credits for the tax paid to Montana on those particular income items. This appeal has been taken from respondent's denial of those claims for refund.

Under section 18001 of the Revenue and Taxation Code, a California resident is allowed a credit against his California

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income tax liability for net income taxes imposed by and paid to another state on income also taxable under California law. Subdivision (a) of section 18001 limits the availability of such a credit as follows:

The credit shall be allowed only, for taxes paid to the other state on income derived from sources within that state which is taxable under its laws irrespective of the residence or domicile of the recipient.
(Emphasis added.)

Appellant argues that respondent's **determination as to the source of the income and the corresponding availability of a credit** should be in conformity with Montana's conclusion that the interest received by appellant on the promissory notes, which he held constituted income derived from business-sources within Montana. Respondent's disallowance of the credit is based on its **conclusion** that, notwithstanding Montana's characterization of the income and its source, under California law **this interest is income derived from California sources, i.e., the promissory notes held by appellant here in California.**

Relevant discussion of an analogous issue is to be found in Miller v. McColgan, 17 Cal. 2d 432 [110 P.2d 419]. The Supreme Court of California there held that dividend income received by a California resident from his stock holdings in a Philippine corporation had its source in the stock itself. Applying the common law doctrine generally followed in determining the taxable **situs** of intangible assets, mobilia sequuntur personam ("moveables follow the person"), the Court concluded, that the taxpayer's California residence combined with his ownership of the stock giving rise to the dividends caused that income to have its source in California. No credit was available, therefore, for income taxes paid to the Philippine Islands on that same **dividend** income.

In arriving at its conclusion, the Court pointed out that though a dividend may have its ultimate source, in the corporation and its activities, its immediate **source, so far as the shareholder is concerned, is his share of stock**, and it is this immediate source which is referred to in the California tax credit provision. (Miller v. McColgan, **supra**.)

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Similarly, the immediate source of interest income upon a debt is the debt itself. Since the debt is an **intangible** property right which has its **situs** at the domicile of its owner, the creditor (Hinckley v. County of San Diego, 49 Cal. App. 668 [194 P. 77]), the interest has its source at that domicile under the mobilia rule as enunciated in the Miller case.

A well established exception to the mobilia doctrine in this state is the "business **situs**" rule, which applies where intangibles are used in connection with a business located outside the state of domicile of their owner. (Westinghouse Co. v. Los Angeles, 188 Cal. 491 [205 P. 1076].) The "business **situs**" exception applies only where there is a general, or more, or less continuous course of business or series of transactions, as distinguished from mere **sporadic** and isolated transactions. (Hinckley v. County of San Diego, supra.) The promissory notes involved here resulted from a single, isolated sale of property, 'They were physically present in California during the taxable years in question in the possession and control of their owner, a resident of this state, and there is no **evidence** that they were being used in connection with any business in Montana.

Although the State of Montana has determined that under its law the interest was derived from sources in Montana, we must be guided by principles developed in our California **courts** in connection with California tax law. The following statement in Miller v. McColgan, supra, 17 Cal. 2d 432 [110 P.2d 419], is applicable here:

That the Philippines may impose such a tax does not mean that under our theories and our act such income is derived from the Philippines. Rather it simply indicates that the Philippines have adopted a theory and philosophy of taxation different from that adopted by California... (17 Cal. 2d 432, at 444.)

In accord with the foregoing analysis it is our conclusion that appellant is not entitled to a credit for income taxes paid to Montana upon the interest income derived from the **promissory notes** which he held.

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ORDER.

Pursuant to the views expressed in the opinion of . . . the board on **file** in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND **DECREED**, pursuant to section 19060 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in **denying the** claims of, **Hallie L. Bills** for refund of personal income tax in the amounts of \$226.58 and \$103.52 for the **years** 1960 and 1961, **respectively**, be and the same is hereby sustained.

Done at Pasadena, California, this 5th day of April- , 1965, by the State Board of Equalization.

John W. Lynch, Chairman
Chas. H. Hensley, Member
John R. Loebe, Member
Richard H. Stein, Member
_____, Member

ATTEST:

W. H. Green, Secretary